



REVENUE ...  
*Working For You*

# **Sales and Use Tax Guide**

December 2004

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Dear Tennessee Taxpayer,

This publication is designed to help taxpayers better understand the Tennessee sales or use tax, including the collection and remittance of the tax. The sales or use tax is an essential part of the Tennessee tax structure. You may find compliance easier when you know more about the tax. Please take time to acquaint yourself with how this tax applies to you. This sales or use tax guide is intended as an informal reference for taxpayers who wish to gain a better understanding of Tennessee sales or use tax requirements. It is not an all-inclusive document. The tax guide is not intended as a substitute for Tennessee sales or use tax statutes or Rules and Regulations, nor is it intended to be a statement of Department of Revenue policy. The information in this guide is current as of the date of publication but could change as the tax laws, their interpretation, and their application do change from time to time because of legislative action, reviews, and court decisions.

Periodically, registered taxpayers are mailed information letters with updates on tax laws and policies. Be sure to read any letter you receive carefully; this information may save you time and money. Informational publications are also available for specific industries. Contact the Taxpayer Services Division to obtain these publications.

The Department of Revenue offers a toll-free tax information line for Tennessee residents. The number is (800) 342-1003. If calling from Nashville or outside Tennessee, you may call (615) 253-0600. The Department of Revenue also offers a telecommunications device for the deaf (TDD) line at (615) 741-7398.

In addition, the Department of Revenue offers a hot line number for the exclusive use of the tax practitioner. In-state practitioners may call toll-free (800) 397-8395; from Nashville and outside Tennessee, call (615) 253-0700.

If you have questions, please do not hesitate to contact any of the offices listed below.

Sincerely,

Taxpayer Services Division

Tennessee Department of Revenue  
Taxpayer Services Division  
Andrew Jackson Building, 3<sup>rd</sup> Floor  
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Toll-free: (800) 342-1003  
Out-of-state: (615) 253-0600  
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#### Regional Offices

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Room 405-B  
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**NOTE:** Public Chapter 357, Acts of 2003, the Streamlined Sales Tax Act, which will become effective no sooner than July 1, 2005, creates significant changes to the Tennessee sales and use tax and the manner in which the sales and use tax is collected. The Act also will remove certain items from the sales and use tax and subject them instead to a privilege tax. The Department of Revenue is currently working on guidance to assist taxpayers in the transition to the Streamlined Sales Tax. That information will be available to the taxpayers in the future.

## SALES OR USE TAX

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### SALES OR USE TAX (Tenn. Code Ann. Sections 67-6-102, 202)

The sales or use tax is a combination of a state tax (7%) and a local option tax (which varies from 1% to 2.75%) imposed by city and/or county governments. This tax is generally applied to the gross sales of any business, organization, or person engaged in retail sales, including the selling, leasing, or renting of tangible personal property and the selling of taxable services not exempt by law. In addition, there is a state single article tax rate of 2.75%, which is discussed on page 9.

Tangible personal property and taxable services specifically intended for resale or sales to a government or sales and use tax-exempt agency are included in total reported gross sales, but are not included in the net taxable total sales.

The “sales price” of an item of tangible personal property is the total amount for which property is sold, including the cost of any services that are part of the sale of the tangible personal property. The tax is imposed on the gross proceeds of leases and rentals of tangible personal property, the gross charge for taxable services, and the gross receipts or proceeds of sales of amusements. For example: A consumer buys four automobile tires subject to the sales or use tax and is charged a fee for mounting the tires on the automobile. The fee for mounting the tires is also subject to the sales or use tax.

The term “sales price” does not include:

- + Dealer cash discounts allowed on property or services purchases. Manufacturer rebates are included in the tax base.
- + Interest charges on purchases bought on an installment plan.
- + Any federal retail excise tax for off-road diesel fuel or any federal excise tax imposed under Sections 4051-4053 of the Internal Revenue Code of 1954.
- + The value of items taken as “trade-ins” on the purchase of similar new or used items. The trade-in item must be listed as such, by model and serial number, where applicable on the customer’s invoice. (Tenn. Code Ann. Section 67-6-510)

There are some exceptions to the 7% standard state sales or use tax rate:

- + The 7% state tax rate does not apply to sales of food and food ingredients as defined in the law. These items are taxed at a state rate of 6%. What constitutes food and food ingredients is addressed on pages 10 and 11.
- + Aviation fuel actually used in the operation of aircraft motors is taxed at 4.5%. (Tenn. Code Ann. Section 67-6-217)
- + Electricity and liquefied gas sold to farmers and nursery operators for production of food, fiber, and horticultural products, and energy fuels sold to nurseries and greenhouses is taxed at the rate of 1.5%. (Tenn. Code Ann. Section 67-6-218)
- + In-state sales of property to common carriers for use outside Tennessee are taxed at the rate of 3.75%. (Tenn. Code Ann. Section 67-6-219)
- + When sold to or used by manufacturers, water will be taxed at 1%, and gas, electricity, fuel oil, and other energy fuels is taxed at a rate of 1.5%. (Tenn. Code Ann. Section 67-6-206)
- + Interstate and international telecommunication services sold to businesses are taxed at a rate of 7.5%. (Tenn. Code Ann. Section 67-6-221)
- + Gross receipts from the sale of manufactured homes, including accessories, furnishings, and delivery or installation fees, are taxed at half the state tax rate which currently equals 3.5%. (Tenn. Code Ann. Section 67-6-216)
- + Cable or wireless cable television services are taxed at a state rate of 8.25% on all charges of \$15.01 - \$27.50. Charges of \$27.51 and higher are taxed at the regular state and local sales or use tax rates. (Tenn. Code Ann. Sections 67-6-103(f), 67-6-226)
- + Direct-to-home satellite services are taxed at a state rate of 8.25% on the total gross charge for subscriptions to television programming. (Tenn. Code Ann. Section 67-6-227)

Tennessee vendors must indicate in specific ways whether customers are paying sales or use tax. If the purchase price of a product includes the tax, it must be indicated in writing on the invoice, on a sign posted in the business, or in a manner that is assured to make the customer aware of that fact. (Tenn. Code Ann. Section 67-6-503)

### Local Option Sales or Use Tax

Any county or incorporated city may levy a tax on the same privileges that are subject to the state’s sales or use tax; all counties and some incorporated cities have adopted a local option tax of up to 2.75%. The local tax is imposed in the locality where water and telephone services are delivered to the consumer or where the dealer of other tangible personal property or services is located. (Tenn. Code Ann. Section 67-6-702)

## SALES OR USE TAX

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### **SALES OR USE TAX (cont'd)** **(Tenn. Code Ann. Sections 67-6-102, 202)**

The law limits some local option tax rates:

There is no local option tax on electric power or energy, natural or artificial gas, coal, or fuel oil.

The local tax rate for water sold to manufacturers is 0.5%. If the local tax rate is less than 1%, the rate for water sold to manufacturers is 0.33%. (Tenn. Code Ann. Section 67-6-702)

The local tax rate for sales in Tennessee of tangible property to common carriers for use outside Tennessee is 1.5%. (Tenn. Code Ann. Section 67-6-702)

Intrastate telecommunication services are taxed at a flat 2.5% local tax rate regardless of the local tax rate levied by the local jurisdiction. (Tenn. Code Ann. Section 67-6-702)

Interstate and international telecommunication services sold to businesses are exempt from local tax. (Tenn. Code Ann. Section 67-6-702)

Interstate and international telecommunication services sold to persons other than businesses are taxed at a flat 1.5% local tax rate regardless of the local tax rate levied by the local jurisdiction. (Tenn. Code Ann. Section 67-6-702)

Cable television programming services provided by a cable television provider or wireless cable television provider offered for public consumption are exempt from local tax up to an amount of \$27.50. (Tenn. Code Ann. Section 67-6-714)

Vending machine sales will be reported on both food and non-food items and are taxed at a flat local tax rate of 2.25% regardless of the local tax rate levied by the local jurisdiction.

### **Who Must Have a Sales or Use Tax Registration? (Tenn. Code Ann. Sections 67-6-102, 201, 211, 602)**

A person or company wishing to manufacture, distribute, sell, rent, or lease tangible personal property, or provide taxable services, in this state must hold a Certificate of Registration in order to conduct business in Tennessee. Business may be conducted by:

- + Selling, renting, or leasing, even by a transient vendor, any type of tangible personal property.
- + Selling any type of taxable service in the state.
- + Furnishing property or services that are subject to the sales or use tax.
- + Charging admission, dues, or fees that are subject to the sales or use tax.
- + Using tangible personal property not previously taxed.
- + Selling any item from a vending machine or device in which merchandise is provided upon deposit of money. A gross receipts registration is also required for sales from certain vending machines operated for the benefit of tax-exempt organizations.

This requirement applies whether your business is a sole proprietorship, partnership, LLC, corporation, or any other type organization including those that are not for profit. Retailers from other states that maintain a physical location in Tennessee, whether temporary or permanent, must also hold a Certificate of Registration. A business having more than one location must hold a certificate for each business location. For example: a clothing business with locations in two malls must hold a certificate for each location.

Dealers having average monthly gross sales of \$400 or less and taxable services of \$100 or less, may, at the discretion of the commissioner, be required to pay tax to their suppliers on purchases in lieu of registering for sales or use tax purposes. For these taxpayers, the department's cost of administering the account would exceed the taxes reported.

### **Who Is Liable For Sales Tax? (Tenn. Code Ann. Sections 67-6-501, 502)**

In Tennessee, the responsibility for sales tax rests primarily on the dealer making retail sales of personal property or services. The law requires that the dealer pass the tax on to the customer, but failure to do so does not relieve the dealer of the responsibility of timely payment of the tax to the state. Either dealers or consumers can be responsible for the tax where consumers have claimed exemptions incorrectly.

In the case of a property management company hired to manage vacation lodging for an individual property owner, the sales tax will be

## SALES OR USE TAX

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### **SALES OR USE TAX (cont'd)** **(Tenn. Code Ann. Sections 67-6-102, 202)**

imposed on the gross charge for rental and will be reported and remitted by the property management company.

Tax will be reported and paid each month based on the gross sales of all taxable personal property or services and purchases subject to use tax during the preceding month. The tax is will be paid on the return for the month in which the taxable event occurs, even if the tax is not collected from the customer during that month. For example: A charge sale is made during the month of June. The dealer must pay the tax on the June return even though the customer may not pay the account until July.

### **Who Is Liable For Use Tax? (Tenn. Code Ann. Section 67-6-203)**

When a user of tangible personal property does not pay tax to a dealer, the user becomes personally liable for the tax. This generally occurs when a user purchases articles from an out-of-state dealer not registered for Tennessee tax. It also occurs when a dealer withdraws inventory items purchased on a resale certificate for business or personal use. For example: A clothing store owner purchases clothing on a resale certificate then takes items from inventory for personal use. Use tax is then due on that clothing.

The use tax rate is equal to the sales tax rate on both the state and local level. Use tax is due when a citizen imports tangible personal property into Tennessee for use. For example: A business relocating to Tennessee brings property into Tennessee purchased in a state with no sales or use tax. The dealer would be liable for use tax on this property. (Tenn. Code Ann. Section 67-6-210)

Use tax is normally incurred when:

- + Purchasing a product in another state without paying sales or use tax and bringing it into Tennessee for use here. (Tenn. Code Ann. Section 67-6-210)
- + Purchasing a product from a mail order catalogue or the Internet and paying no sales or use tax. (Tenn. Code Ann. Section 67-6-210)
- + Purchasing a product from a transient business that does not collect sales or use tax. (Tenn. Code Ann. Section 67-6-210)

- + Consuming or using a product that was purchased without paying sales or use tax. (Tenn. Code Ann. Section 67-6-203)
- + Consuming, as a service provider, taxable services or tangible products in the performance of a service. (Tenn. Code Ann. Section 67-6-316)

### **How to Register (Tenn. Code Ann. Sections 67-6-601, 602)**

#### **Tennessee Retailers**

Perhaps the best method of applying for the Certificate of Registration is to register online at <http://www.tennesseeanytime.org/bizreg/>. You may also visit one of the Department of Revenue offices listed on the inside front cover of this publication. Trained personnel are available there to explain Tennessee's tax system and answer any of your questions.

Whether registering online, in person, or by mail, you must have the following information to complete your application:

- + The name, address, and phone number of the business, all owners, officers, or partners, and the person making the application.
- + The Social Security Number(s) of the owner(s), partners, or officers.
- + The Federal Employer's Identification Number (FEIN) issued by the U.S. Internal Revenue Service if you have one.
- + A description of the business, the type of ownership, a brief explanation of the nature of the business, and, if the business is a corporation, the date of incorporation.
- + If you have purchased your business, the name and address of the previous owner.
- + The signature, on the application, of the sole proprietor, a partner, or an officer of a corporation.

#### **Out-of-state Retailers**

Out-of-state retailers must register with the Department of Revenue and obtain a Certificate of Registration for payment of the sales or use tax if they have a "nexus" in Tennessee. Retailers are considered to have a nexus if they:

- + Have an office, distribution point, sales room, warehouse, or any other temporary or permanent place of business in Tennessee.
- + Have an agent, salesperson, canvasser, or solicitor operating in Tennessee for the



## SALES OR USE TAX

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### **SALES OR USE TAX (cont'd)** **(Tenn. Code Ann. Sections 67-6-102, 202)**

- purpose of making sales or taking orders for sales.
- + Furnish any property or services subject to the sales or use tax while in Tennessee.
- + Are the lessors of tangible personal property located in Tennessee.
- + Are construction contractors performing jobs in Tennessee.
- + Have any other physical presence in Tennessee.

This requirement applies even though the sale of the product or its delivery is in interstate commerce. For example: An out-of-state computer company sells computer systems to Tennessee businesses through a salesperson that travels in this state. This business is required to obtain a Certificate of Registration and collect sales or use tax on the price of the system.

A business having a physical presence in Tennessee must collect and remit sales or use tax on all sales whether orders are taken in person, by phone, or by mail.

Mail order companies that do not have a physical presence, either permanent or temporary, cannot be held responsible for collecting and remitting sales or use tax. They can voluntarily register to collect the tax for their customers. However, if they do not collect and remit the sales or use tax to the state, then the consumer is responsible for reporting and paying the tax. Use tax is due on products purchased from companies not registered to collect the Tennessee sales or use tax.

### **Revocation of Certificate of Registration** **(Tenn. Code Ann. Sections 67-6-603, 604)**

Any taxpayer violating the provisions of the sales or use tax law may have the certificate of registration revoked by the Commissioner after an opportunity for a due process hearing has been afforded. If the certificate is revoked, that person will not be eligible to apply for another certificate for 12 months. The taxpayer is entitled to a hearing with the department to determine if revocation was justified. The taxpayer will receive a 10-day notice of the

hearing and be allowed to present evidence as to why the certificate should not be revoked.

Any person engaging in business as a dealer in Tennessee without a certificate of registration from the department is guilty of a Class C misdemeanor. (Tenn. Code Ann. Section 67-6-606)

### **Changes in Ownership, Address, or Business** **(Tenn. Code Ann. Section 67-6-602)**

You must notify the Department of Revenue if the business ownership changes in any manner. This change could be selling or closing the business, adding or changing partners, transferring or changing the ownership of the business, or changing corporate structure requiring a new charter or certificate of authority. You must also notify the Department of Revenue if the business location changes.

If any of the changes mentioned should occur, answer the questions on the back of the business's Certificate of Registration and mail it to the Department of Revenue. The new owners or officers, if applicable, must then apply for a new Certificate of Registration.

If you sell your business or go out of business, you must make a final sales or use tax return and pay all sales or use tax due within 15 days after the date you sold or quit the business. If you sold the business, the purchaser must apply for a Certificate of Registration in his or her own name. (Tenn. Code Ann. Section 67-6-513)

### **Additional References**

For additional information, or to view actual documents pertaining to Tennessee's tax laws, we invite you to visit these Internet Web sites:

For the Tennessee Code, as well as information or changes to the Sales or Use Tax law, Revenue Rulings, Important Notices, Answers to Frequently Asked Questions, and Tax Forms, visit the Department of Revenue's Web site: <http://www.Tennessee.gov/revenue>.

For tax Rules and Regulations, see the Secretary of State at [www.state.tn.us/sos/rules/rules.htm](http://www.state.tn.us/sos/rules/rules.htm).

## SALES OR USE TAX

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### DEFINITIONS

#### **Occasional and Isolated Sales** (Tenn. Code Ann. Section 67-6-102)

Occasional and isolated sales, also known as casual and isolated sales, are sales made by persons not in the business of regularly selling the type of property being sold. These sales are not subject to tax. Occasional and isolated sales are also sales of tangible property taking place only during temporary sales periods of 30 days or less and occurring no more than twice per year. Example: the sale of a piece of furniture in a yard sale and the sale of Girl Scout cookies are considered occasional and isolated sales.

Any church or similar organization that regularly sells goods or taxable services is considered a dealer by the Department of Revenue and, generally, will be liable for tax on those sales. Sales of motor vehicles, boats, and airplanes are not considered occasional and isolated sales in sales tax law.

Property of a sole proprietorship that becomes property of a corporation as a result of incorporation of the sole proprietorship is not subject to tax. (Tenn. Code Ann. Section 67-6-223)

#### **Single Article** (Tenn. Code Ann. Section 67-6-702(d))

The term “single article” refers to any item that is considered, by common understanding, to be a separate unit, apart from any accessories, extra parts, etc., that is capable of being sold as an independent item or as a common unit of measure. Independent units sold in sets, lots, suites, or such groupings, are not considered to be single articles. The local option tax cannot exceed 2.75% and may be assessed only on the first \$1,600 of the purchase price of any single item of tangible personal property. Some applications of the “single article” concept are:

#### **Motor Vehicles**

Parts and accessories for motor vehicles that are installed at the factory and delivered as original equipment will be treated as part of the unit. Likewise, parts and accessories that are installed by the dealer or distributor prior to, or at the time of, sale and are included in the sale price will

be considered as part of the unit. This also applies to parts or equipment required to be installed prior to the sale for state or federal law.

#### **Boats**

Boat motors and any dealer installed accessories that are installed prior to the sale, freight, and labor, excluding trailers, will be treated as part of the boat unit in the same manner as parts and accessories for motor vehicles are treated. Items such as skis, ski ropes, personal flotation devices, and similar items are not considered part of the single item. Boat trailers will be taxed as a separate single item. The state tax rate applies to the total bill of sale.

#### **Manufactured Homes**

Parts, accessories, furniture, appliances, and other items that are part of a manufactured home at the time of sale are treated as parts of the single unit for the local tax liability. Also included as part of the single article price are delivery fees, installation fees, and other incidental items that are part of the sale. Installation includes charges made for setup, plumbing hookup, and electrical hookup.

#### **State Tax on Purchases of Single Articles**

Effective July 15, 2002, an additional state sales or use tax at the rate of 2.75% was enacted on the portion of the sales price, from \$1,600.01 up to and including \$3,200, of any single article sold. This is a state tax only. This portion of the sales price is not subject to the local tax.

#### **Tangible Personal Property** (Tenn. Code Ann. Sections 67-6-102, 212)

Tangible personal property is defined as property that may be seen, weighed, touched, felt, or is perceptible to the senses in any other manner. Prepaid telephone calling cards and authorization numbers are considered tangible personal property. Computer software is also considered to be tangible personal property. Tangible personal property does not include stocks, bonds, notes, insurance, and other securities. It does not include signals broadcast over the airwaves. It also does not include utility poles, anchors, guys, and conduits, which are defined to be real property.

## SALES OR USE TAX

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### FOOD AND FOOD INGREDIENTS (Tenn. Code Ann. Section 67-6-228)

Although the general sales or use tax rate increased on July 15, 2002, sales tax law provides that sales of food and food ingredients remain subject to a state rate of 6% plus the applicable local tax rate.

#### What Are “Food Or Food Ingredients?”

In specifying that food and food ingredients remains at the 6% state rate, the law defines “food and food ingredients” to mean “substances, whether in liquid, concentrated, solid, frozen, dried, or dehydrated form, that are sold for ingestion or chewing by humans and are consumed for their taste or nutritional value.” Food and food ingredients do not include beverages containing alcohol and products containing tobacco.

The law also specifies that the 6% rate does not apply to candy, dietary supplements, or prepared food.

#### Examples Of “Food Or Food Ingredients”

The following is a partial listing of items that meet the requirements to be considered food and food ingredients and are subject to the 6% state rate, if not prepared by the seller. This list is not all-inclusive.

Baking powder, baking soda, bread, cakes and pies, cereal, chip dip, chips, cocoa and beverage powders other than dietary supplements, coffee, condiments, cookies, cooking oil, dairy products, fruit (fresh or dried), eggs, fish and meats, flour, frozen meals, fruit juices, gelatin, gravies and sauces, herbs and spices, ice cream, sherbet, frozen yogurt, ice, margarine and shortening, nuts, popcorn, poultry, pumpkins, raisins, relishes, salad dressing, salt and pepper, soft drinks, sugar, sweeteners, vegetables, tea, and water.

The following is a partial list of items that are not considered food or food ingredients and are taxed at the 7% rate. This list is not all-inclusive.

Beer, wine, alcoholic beverages, cigars, cigarettes, chewing tobacco, cough drops, throat

lozenges, breath sprays or strips, toothpaste, rock salt, and block or dry ice.

#### Items Not Taxable At The 6% Food Rate

##### Candy

“Candy” is defined as a preparation of sugar, honey, or other natural or artificial sweeteners in combination with chocolate, fruit, nuts, or other ingredients or flavorings in the form of bars, drops, or pieces. Candy does not include any preparation containing flour and must require no refrigeration. If an item requires refrigeration or has the word “flour” as an ingredient on the label, it is not candy.

Examples of items that are considered to be candy (the list is not all-inclusive) are breath mints; candy bars; chocolate chips; fruit roll-ups; marshmallows; caramel corn; caramel apples; chocolate or carob covered raisins or nuts; sweet or semi-sweet cooking bars or chips; gum; honey roasted or beer nuts; trail mix that includes candy; peanut brittle; sugarless candy; and yogurt covered raisins or nuts.

##### Dietary Supplements

In order to be considered a dietary supplement, a substance must meet all of these criteria:

“Dietary supplements” contain one or more of the following dietary ingredients: a vitamin; a mineral; an herb or other botanical; an amino acid; a dietary substance for use by humans to supplement the diet by increasing the total dietary intake; or a concentrate, metabolite, constituent, extract, or combination of the ingredients listed.

Dietary supplements are also intended for ingestion as a tablet, capsule, powder, softgel, gelcap, or liquid form. If it is not intended for ingestion in one of these forms, it is not represented as conventional food and is not represented to be the sole item of a meal or diet.

Dietary supplements must be labeled as a dietary supplement, identifiable by the “Supplement Facts” box found on the label and required by federal regulations. Any item that is required to have a “Supplement Facts” label is

## SALES OR USE TAX

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### FOOD AND FOOD INGREDIENTS (cont'd)

taxable at the full 7% state rate plus the applicable local rate. These items include amino acids; antioxidants; bee pollen; enzymes; garlic capsules; ginseng; herbal supplements; immune supports; lecithin; metabolic supplements; vitamins and minerals; and zinc lozenges. This list is not all-inclusive.

#### Meal Substitutes

Meal substitutes are taxable at the 6% state rate and applicable local rate. Meal substitutes are labeled with "Nutrition Facts" and include unsweetened breakfast bars or those containing flour; unsweetened dried fruit snacks; drinks such as Ensure or Boost; pop tarts; and soup mixes. This list is also not all-inclusive.

#### Prepared Food

"Prepared food" is food that is sold in a heated state or that is heated by the seller; food where two more food ingredients are mixed or combined by the seller for sale as a single item; or food sold with eating utensils, provided by the seller, such as plates, knives, forks, spoons, glasses, cups, napkins, or straws. The seller may prepare the item where the food is sold or at another location.

The term "seller" means the legal entity that sells the product at retail. If the seller prepares and sells the food item, the item is taxed at the 7% state rate plus the local option rate. If the seller contracts with another legal entity to prepare the food, the food is not prepared by the seller and is taxed at the 6% state rate plus the local option rate, unless the legal entity preparing the food is an agent of the seller.

Food that is only repackaged, pasteurized, or sliced by the seller is not considered to be prepared food. Serving size or quantity does not affect the taxability of a food item.

Examples of prepared food items taxable at the 7% state plus local rate are any food item sold in a heated state, if prepared by the seller; bakery goods made by the seller; cold or frozen meals, and soups, that are ready to heat and eat, fruit trays, cookie dough, coffee or tea prepared by the seller; combined raw meats, ice cream in cones, sundaes, or such preparations; uncooked meatloaf; marinated raw shrimp; party trays; pizza, either baked or uncooked; ready to eat meats, poultry, or fish (cooked, smoked, or dried such as summer sausage, beef or venison sticks, and smoked fish); rotisserie chicken; salad greens mixed by the seller; salads and other deli dishes; sandwiches; soups, casseroles, or meals sold warm and ready to eat; warmed or honey roasted nuts.

Food that is not prepared by the seller, but is sold with eating utensils provided by the seller, is prepared food and is taxable at the 7% state rate plus the applicable local rate. Eating utensils include, but are not limited to, plates, knives, forks, spoons, glasses, napkins, cups, and straws. Box lunches with straws, napkins, plastic forks, and other utensils are considered prepared food. If the manufacturer, rather than the seller, provides an eating utensil with the food, that food is not considered prepared food and is taxable at the 6% state rate plus the applicable local rate. For example, a box of crackers with cheese spread that comes with a plastic spreader is subject to the 6% state tax plus the applicable local tax because the spreader is not provided by the seller.

## SALES OR USE TAX

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### TAX CREDITS

#### **Credits (Tenn. Code Ann. Section 67-6-507)**

If a consumer voluntarily returns articles of property to a dealer after the sales or use tax has been collected and remitted, the dealer may deduct the sales price of that property from the taxable transactions shown for the current month's return. The dealer must maintain records clearly indicating that the price of the item plus the sales or use tax was refunded to the consumer.

A dealer who repossesses, or enforces a lien against, property the dealer has sold, on which there is an unpaid balance of greater than \$500, may deduct on the current report an amount equal to the unpaid balance minus \$500. The amount of unpaid balance does not include interest, carrying charges, or other similar charges. The dealer must document the credit by maintaining records on the parties and items involved, dates of the sale and the repossession, the original purchase price, and the amount of the unpaid balance.

Auto body paint shops may take a credit of 100% of the cost of equipment purchased to comply with governmentally imposed pollution control standards. Dry cleaners may take a credit of 50% on replacement equipment purchased to comply with governmentally imposed pollution control standards. Application must be made to, and approval received from, the Department of Revenue. Those businesses taking either credit will provide documentation that the equipment was necessary for compliance with current standards.

*A credit or refund is also available to anyone purchasing pollution control equipment required by law that is used to treat pollution created by the taxpayer. The credit does not apply to taxpayers that primarily treat pollution created by others. (Tenn. Code Ann. Section 67-6-346, amended by Public Chapter 924, Acts of 2004)*

A dealer who has paid the sales or use tax on a sale to an account that later becomes a bad debt and is charged off for federal income tax purposes may take the amount of that sale as a credit on the current report. If that account is then paid to the dealer, the dealer will report the amounts paid in the next regular return and the tax amount due.

There is a credit of the amount of any special contractor tax paid in another state for the sale of materials used by fire protection sprinkler contractors for fabrication of pipe and pipe fittings or use valves and pipe fittings in the performance of out-of-state contracts. The credit will be limited to the tax on the value of the materials. (Tenn. Code Ann. Section 67-6-355)

#### **Sales or Use Tax Paid in Another State**

Persons having paid a legally imposed sales or use tax to another state on tangible personal property imported into Tennessee may claim that payment as a credit against any use tax liability in this state. If the tax paid was less than what is due in Tennessee, the taxpayer will be liable for the difference. (Tenn. Code Ann. Section 67-6-507)

Residents of other states who move to Tennessee and import their automobiles, personal effects, and household goods into the state are not liable for use tax on these goods purchased prior to the relocation. This does not apply to property imported for business purposes. (Tenn. Code Ann. Section 67-6-210)

## SALES OR USE TAX

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### TAXABLE AND NON-TAXABLE PROPERTY AND SERVICES

#### Taxable Tangible Personal Property (Tenn. Code Ann. Sections 67-6-102, 212)

Generally, most sales, leases, or rentals of tangible personal property are taxable under the Tennessee sales and use tax law. Examples are:

- + Items sold by grocers to consumers at retail.
- + Clothing and other items of personal apparel.
- + Motor vehicles and marine vessels including repair parts and accessories.
- + Watches, rings, and other items of jewelry.
- + Building materials sold at retail or to realty contractors.
- + Supplies sold to and consumed by dentists and veterinarians.
- + Furniture, appliances, and home furnishings.
- + Electronic equipment and supplies.
- + Computer hardware, software, and peripherals.
- + Souvenirs, gifts, and novelty items.
- + Books, magazines, and other periodicals.
- + Sales and recharging of prepaid telephone calling cards.
- + Cellular phones and pagers.
- + Prepared meals and beverages purchased from restaurants.
- + Water, gas, and electricity.

This list is not intended to be all-inclusive. There are many other items of tangible personal property that are subject to the sales or use tax.

*Charges for delivery or shipping where the consumer takes possession of the item being shipped at the destination point are considered a part of the sales price and the charge is subject to tax if the sale of such property is subject to tax. If the consumer takes possession at the point of origin, shipping charges are not considered a part of the sale price and are not subject to tax.*

#### Services

Most services are not subject to the sales tax. However, some services are specifically named in the law as being subject to the tax. The following examples are services that are taxable under Tennessee law. While not necessarily all-inclusive, this list may assist you in determining if the service is taxable. Please contact the Department of Revenue if you have questions about any specific service.

#### Taxable Services (Tenn. Code Ann. Section 67-6-102)

Charges for the use of rooms or accommodations furnished for periods of less than 90 days by hotels, motels, inns, or other tourist lodgings. The tax does not apply to accommodations or rooms furnished to the same person for 90 or more continuous days

Charges for services rendered in the operation of parking or vehicle storage facilities. The tax does not apply for parking in state and local government facilities or on the street where the fees are collected by state or local government parking meters.

Charges for furnishing intrastate, interstate and international telecommunications services that are sourced to Tennessee.

Charges for repair services of tangible personal property such as automobiles, business machines, and appliances. Charges for warranty or service contracts, provided that repairs performed under such contracts are not also subject to tax.

Charges for laundry and dry-cleaning services to tangible personal property except for coin-operated facilities.

Charges for bathing and grooming animals. This service is taxable only on 15% of the total charge. There is no tax applied to bathing performed by a licensed veterinarian as a part of the practice of veterinary medicine. There is no tax on grooming services billed separately.

Charges for installation of items of tangible personal property that remain tangible personal property after installation. For example: A retailer charges a fee for the setup of computer hardware in the buyer's home. This service is taxable under the sales tax.

Charges for renting space to a dealer with no permanent location in Tennessee or to a dealer registered for sales in another part of Tennessee but making sales at this location on a temporary basis. This does not include space rental at flea markets, craft fairs, or antique malls. This does not include gun shows or book fairs sponsored



## SALES OR USE TAX

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### TAXABLE AND NON-TAXABLE PROPERTY AND SERVICES (cont'd)

by nonprofit organizations. This also does not include conventions, trade shows, or expositions that do not allow the general public to make sales in the exhibit area.

Also taxable under Tenn. Code Ann. Section 67-6-212 are charges for a variety of amusement, recreation, and entertainment activities such as:

- + Membership dues to sports and recreation clubs or health spas.
- + Admissions to sporting events, musical and theatrical performances, and other amusements except as exempted by law.
- + Charges for entering or engaging in any kind of recreational activity.
- + Charges for using tangible personal property for amusements, sports, entertainment, or recreational activities such as golf carts, tennis courts, or bowling shoes.
- + Complimentary dues and fees, with a value equal to the normal cost, except when provided to students at a public school or university.

#### Non-taxable Tangible Personal Property

Many items of tangible personal property are specifically exempted from the sales or use tax by Tennessee law. Other items are exempted when purchased by certain entities or for certain purposes. These items and entities are discussed in following portions of this publication.

### Non-taxable Services

Examples of some non-taxable services in Tennessee are:

- + Furniture moving.
- + Barber and beauty shop services.
- + Hospital, physician, and dental services.
- + Carpet cleaning.
- + Window washing.
- + Taxidermy services.
- + Use of recording studios and television studios.
- + Furnishing of equipment when the owner provides a person, or crew, to operate it. Continuous supervision and control are required.
- + Carpentry, painting, and carpet installing.
- + Lawn mowing.

However, sales of goods or property to these providers that are consumed or used in the performance of their services are subject to the sales or use tax. Any items of tangible personal property sold by these providers, separately from their services are also subject to the sales or use tax.

These listings of taxable and non-taxable property and services are not necessarily all inclusive. The tax laws in Tennessee are also amended from time to time; some items may be added or deleted. Any questions concerning the taxability of tangible personal property or services should be directed to the Taxpayer Services Division.

## SALES OR USE TAX

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### EXEMPTIONS REQUIRING CERTIFICATES

Three general types of exemptions are provided in Tennessee sales or use tax law. These are exempt entities, exempt items, and exempt transactions. Many exempt transactions and sales to exempt entities require that the purchaser claiming the exemption provide specific documentation to the dealer. The dealer is required to keep the exemption documentation on file to support the exempt sales for audit purposes.

#### Documenting Exemptions

Certificates are used to document authorization for purchasing tangible personal property and taxable services free of tax. These certificates are issued directly to the specific taxpayer upon application to and verification by the Department of Revenue. They are to be given to the seller by the taxpayer wishing to purchase free of tax.

#### **Blanket Certificate of Resale (Tenn. Code Ann. Sections 67-6-102, 602; Sales or Use Tax Rule 1320-5-1-.68)**

Dealers shall require certificates of resale for all tangible personal property sold, or services rendered in this state, for the purpose of resale. These certificates must be available for audit. A dealer duly registered under the provisions of the sales tax law, and continually engaged in the business of selling tangible personal property or taxable services at retail shall not be required to execute additional certificates of resale for individual purchases as long as there is no change in the character of the business operation and the purchases are of tangible personal property or taxable services of the kind usually purchased by the purchaser for resale. This certificate remains good until revoked in writing by the issuer.

All sales for resale that are not supported by resale certificates properly executed shall be deemed retail sales, and the dealer will be held liable for the tax.

Certificates of resale may not be used to obtain tangible personal property or taxable services that would be used by the purchaser, not resold.

Such use will be grounds for the commissioner to revoke the registration certificate of the dealer wrongfully making use of the certificate of resale. In addition to this penalty, it is a misdemeanor to misuse the certificate of registration and resale certificate for the purpose of obtaining tangible personal property or taxable services without the payment of the sales or use tax when due.

For example, it would be proper use of a resale certificate for a candy wholesaler to accept a resale certificate for candy purchased by a grocery store. It is reasonable for the wholesaler to believe the candy will be resold by the grocery store; the sales or use tax will be collected on the final sale to the customers.

However, it would be improper for a furniture dealer to accept a resale certificate for its sale of office furniture to an automobile dealer. The furniture dealer should know the automobile dealer does not sell furniture in the course of the purchaser's normal business; either the seller or purchaser can be held liable for the tax.

If a wholesaler or dealer sells tangible personal property or taxable services free of the sales or use tax on a certificate of resale when that seller knows, or should know in the use of ordinary care, that the property or service being sold is not for resale by the purchaser, but is for the purchaser's own use or consumption in business or otherwise, the registration certificate of the wholesaler may be revoked by proper action of the commissioner. Either the wholesaler or the purchaser can also be liable for the tax.

The commissioner, however, may extend special written permission to a registered dealer to make purchases for the dealer's own use under a certificate of resale, and to report that dealer's tax liability separately to the Department of Revenue. This permission may be extended only under exceptional circumstances or hardship to the taxpayer. A certified, or photostatic, copy of this permission shall be filed with the wholesalers or dealers. This special written permission to remit the use tax shall in no way alter or affect the criteria for determining whether a transaction is taxable in Tennessee.



## SALES OR USE TAX

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### EXEMPTIONS REQUIRING CERTIFICATES (cont'd)

If a buyer purchases for resale and later uses the product rather than reselling it, the buyer is responsible for reporting and paying sales or use tax on the items used. This must be done on the sales or use tax return for the period in which the goods were used.

#### **Certificate of Exemption for Nonprofit Organizations (Tenn. Code Ann. Section 67-6-322)**

This certificate is used by non-governmental organizations, that have been issued a certificate of exemption by the Commissioner of Revenue to purchase free of tax, goods and taxable services that the organization will use, consume, or give away. The certificate will contain an exemption number that is unique to the organization receiving the letter. The dealer making a sale to one of these organizations must maintain a copy of the exemption letter in the entity's files for audit purposes. These organizations include churches, temples, synagogues, mosques, boys' and girls' clubs, universities, colleges, schools, orphanages, foster home institutions, homes for the aged, hospitals, community health councils, volunteer fire departments, organ banks, organizations primarily for the spiritual and recreational environment of the armed forces, state owned historical properties, nonprofit community blood banks, senior citizen centers, certain nonprofit talent and beauty contest corporations, and 26 USC Section 501(c)(3) organizations, (c)(5) labor organizations, (c)(13) nonprofit cemeteries, and (c)(19) war-time veterans' organizations.

When accepting an exemption, the seller must ensure that the purchase is billed to the exempt organization and is paid for with checks or credit cards of the organization.

*These exemptions are subject to a four-year periodic review to determine continuing eligibility. After completion of the four-year review, exemption certificates bearing new effective dates are issued to qualifying entities, and retailers are notified of the new effective date. At that time, previous exemption certificates are no longer valid.*

Out-of-state organizations that hold a federal tax exemption under 26 USC Section 501(c)(3) must submit a copy of their federal exemption letter in lieu of a certificate of exemption from the Commissioner of Revenue. Instate Section 501(c)(3) entities require a Certificate of Exemption issued by the commissioner.

#### **Certificate of Exemption for Qualified Call Centers (Tenn. Code Ann. Section 67-6-356)**

Sales of interstate and international telecommunication services to businesses for operation of one or more call centers are exempt upon presentation of an appropriate exemption certificate issued by the Department of Revenue. Call centers are single locations having at least 250 employee jobs and utilizing telecommunications services in one or more of the following activities:

- + Customer services.
- + Soliciting sales.
- + Reactivating dormant accounts.
- + Fund raising.
- + Conducting surveys or research.
- + Collection of receivables.
- + Receiving or taking orders.
- + Receiving reservations.

## SALES OR USE TAX

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### EXEMPTIONS REQUIRING DOCUMENTATION

Under sales or use tax law, some sales are tax-exempt without the necessity of a certificate issued by the department but do require documentation between the seller and buyer. Examples of the many exemptions that fall under this category are shown below, but this list is not all-inclusive. Dealers should contact the department for more information on the types of exemptions available.

#### Removal from Tennessee by Buyer

Tennessee law allows a buyer to purchase a motor vehicle in Tennessee and have up to three days to remove the motor vehicle to another state without having to pay sales or use tax on the purchase. This exemption applies to all motor vehicles that would be subject to registration and titling in Tennessee were the vehicle to remain in state. This also includes all off-highway motor vehicles as defined in Tenn. Code Ann. Section 55-3-101(c)(2).

There is also a provision under Tennessee law that exempts, from the sales or use tax, the retail sale of boats, motorboats, and other vessels that are subject to registration in this state that are removed from Tennessee to another state within three days after purchase.

When purchasing these items under this privilege, the buyer presents the seller with the Seller/Purchaser Affidavit of Exemption for Motor Vehicles, Boats, and Vessels Sold For Removal From Tennessee Within Three Days indicating the city and state to which the item will be delivered. (Tenn. Code Ann. Sections, 343, 345)

Tennessee law also allows a non-resident buyer to purchase a helicopter or airplane in Tennessee without having to pay sales tax if the aircraft will be located out of state and removed from Tennessee within 15 days of purchase. (Tenn. Code Ann. Section 67-6-313)

When purchasing a helicopter or airplane under this privilege, the buyer presents the seller with the Affidavit of Transfer of Aircraft/Helicopter indicating the aircraft will be removed within 15 days of purchase and the city and state where the aircraft will be located.

#### Exemption for Railroad Track Materials and Locomotive Radiators

This exemption is for railroads seeking to purchase railroad track materials and locomotive radiators for use outside the state of Tennessee as provided in § 67-6-340. If the railroad fails to keep records sufficient to prove these materials were used out-of-state and not within Tennessee, then the railroad will be liable for the sales or use tax on these items. (Tenn. Code Ann. Section 67-6-529)

**Exemption for Electric Cooperatives and Membership Corporations and Utility Districts** – for entities organized under Sections 65-2401, 2501, and 2601, et seq., of the Tennessee Code Annotated.

**Exemption for Electric Generating and Distribution Systems, Resource Recovered Facilities, or Coal Gasification Plants** – for entities created by the federal, state, or local governments under the Electric Membership Corporation or the Electric Cooperative Laws.

## SALES OR USE TAX

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### AGRICULTURAL EXEMPTIONS

#### Farmers and Nurseries Exemption Certificate

In order to qualify for the sales or use tax exemption for the purchase of farm machinery and equipment and electricity and liquefied gas at a reduced rate, the farmer or nursery operator must present a properly completed and signed certificate to the seller. The certificate is the seller's documentation of tax-exempt sales of goods and services to farmers and nursery operators.

As with the Blanket Certificate of Resale, the buyer is obligated to ensure that all goods and services purchased under this certificate are actually purchased for the production of agricultural or nursery products. The seller is also obligated to refuse the certificate on any purchases that obviously do not conform to the requirements for the farm equipment and machinery exemptions. (Tenn. Code Ann. Section 67-6-102)

The Exemption Certificate for Farm Machinery and Equipment and for Purchase of Electricity and Liquefied Gas at a Reduced Rate is the seller's documentation of tax-exempt sales of goods and services to farmers and nursery operators.

#### Agricultural Exemptions (Tenn. Code Ann. Sections 67-6-207, 301, 329)

There are a number of exemptions for farm products, farmers, and nursery operators. The farmer or nursery that purchases agricultural items exempt from sales or use tax must provide a farmer's exemption certificate for the seller's records. Exempted items include:

- + Farm equipment or machinery used for producing agricultural products for sale. The purchase price of these items must be more than \$250. This does include the rental or lease of these items even if the lease price is less than \$250. Automobiles, trucks, household appliances, and tangible personal property that becomes real property upon installation are not included in this exemption.
- + Grain bins that are sold to or used by the farmer.
- + Aircraft designed and used for crop dusting.
- + Equipment that is used solely for harvesting timber.

- + Trailers used for transporting livestock.
- + Self-propelled fertilizer or chemical spreading equipment if not designed for over-the-road use.
- + Environmental control systems for raising poultry.
- + Parts and labor used in the repair of exempt farm machinery.
- + Gasoline or diesel fuel used for "agriculture purposes."
- + Containers for farm products or plastic and canvas used in the care of plants or as cover for grain storage structures.

There are also a number of agricultural exemptions available to any taxpayer. The purchase of these items does not require any type of exemption certificate. These include:

- + Livestock purchased for resale at the close of feeding or grazing season.
- + Feed for livestock, poultry, or other domestic animals usually found on a farm, other than pets, for commercial purposes.
- + Nursery stock produced by nurserymen and sold directly from the nursery, if accounted for separately from other nursery stock.
- + Seeds, seedlings, and cuttings that will produce food, fiber, or tobacco.
- + Fertilizer and pesticides used to aid the growth and development of seeds, seedlings, or plants. Also included are solutions specifically for mixture with pesticides or for use as a soil conditioner.
- + Livestock wormers, medications, and instruments used to administer medications.
- + Any substance used in the reproduction of livestock, including embryos and semen.
- + Agri-sawdust.
- + Any seeds, seedlings, cuttings, fertilizers, pesticides and additives, or containers, canvas, and plastic as previously indicated that are sold directly to a nursery operator.

#### Sales by Farmers and Nursery Operators

Proceeds from the sale of livestock, poultry, nursery stock, or other farm products by the farmer or nursery operator are exempt from the tax. If the farmer or nursery operator produced at least 50% of the products, then 100% of the proceeds are tax-exempt. If the farmer or nursery operator produced less than 50%, then the proceeds from products produced by them are tax-exempt. The 50% test is applied on a calendar year basis.

## SALES OR USE TAX

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### EXEMPTIONS AND REDUCED RATES FOR QUALIFIED MANUFACTURERS

A manufacturer is a business whose principal activity (more than 50%) at a specific location is fabricating and processing tangible personal property for resale and consumption off the premises. A qualified manufacturer enjoys substantial tax benefits. Before receiving eligibility for these exemptions, a manufacturer must file an application with the Department of Revenue and receive an authorization letter with a unique Industrial Machinery Number assigned to each specific manufacturing location. (Tenn. Code Ann. Section 67-6-206)

*Effective June 7, 2004, companies engaged in the repair of aircraft for unrelated commercial or governmental entities may qualify for sales and use tax manufacturing exemptions. (Tenn. Code Ann. Section 67-6-102(a)(9), amended by Public Chapter 924, Acts of 2004)*

#### Industrial Machinery

Industrial machinery is machinery necessary to, and primarily for, fabricating or processing tangible personal property for resale and consumption off the premises. The purchase, lease, or rental of qualified machinery, and its repair and replacement parts, are exempt from the sales or use tax.

Exempt qualified machinery generally includes the machines that transfer raw materials from inventory and begin the processing cycle, process the product through the various phases of manufacture, and transfer the finished product from the final processing step to inventory. Any device that powers this machinery and the oils and lubricants used in the machinery are also tax exempt. (Tenn. Code Ann. Sections 67-6-102, 206)

#### Industrial Machinery Authorization

Before receiving eligibility for these exemptions, a manufacturer must file an application with the Department of Revenue and receive an authorization letter with a unique industrial machinery number. (Tenn. Code Ann. Section 67-6-206)

Once the department approves this authorization, the manufacturer may be entitled to tax-exempt

purchases and service of qualified industrial machinery as well as reduced or tax-exempt purchases of electricity, gas or other fuels and water as provided under the law.

#### Pollution Control Equipment

Pollution control machinery and equipment needed to control or eliminate air and water pollutants resulting from manufacturing are considered industrial machinery. As such, they are tax-exempt to the qualified manufacturer. (Tenn. Code Ann. Section 67-6-102(14))

#### Energy Fuel and Water

Qualified manufacturers are authorized to make purchases at a reduced 1.5% state tax rate on all forms of energy used in any manner on the manufacturing site. This includes electricity, natural gas, coal, firewood, fuel oil, and propane and butane gases. These energy sources are not subject to a local option tax. Any energy fuel that comes into direct contact with the product during manufacturing and is metered separately is tax-exempt. (Tenn. Code Ann. Section 67-6-206)

Manufacturers are also entitled to a reduced state tax rate of 1.0% and a local tax rate of 0.33% to 0.5% on water used within the manufacturing site. Water wetting the product during the manufacturing process that is separately metered is tax-exempt. (Tenn. Code Ann. Sections 67-6-206, 702)

#### Computers (Tenn. Code Ann. Section 67-6-206)

Any computer, including software, which is primarily used to control the operation of industrial machinery, is tax-exempt.

#### Industrial Materials

Chemicals, solvents, greases, and similar items coming into direct contact with the product, becoming a part of the finished product, or being rapidly used in production of the finished product are tax-exempt. Once removed from inventory, these items must be totally used or consumed within 25 days. This exemption is available to all manufacturers and is not subject to the 51% test. (Tenn. Code Ann. Sections 67-6-102(14) & (24))

## SALES OR USE TAX

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### EXEMPTIONS AND REDUCED RATES FOR QUALIFIED MANUFACTURERS

#### Material Handling and Racking Systems Equipment

Material handling and racking systems equipment used in a qualified new or expanded warehouse or distribution facility, purchased beginning 1 year prior to the start of, and ending 1 year after the substantial completion of, the construction or expansion of the facility, not to exceed three years, qualifies for the industrial machinery exemption. An investment of more than \$10 million is required. A taxpayer must submit an application with a plan describing the investment to be made, to the Department of Revenue. If approved, the taxpayer will receive an Industrial Machinery number authorization letter. (Tenn. Code Ann. Sections 67-6-102(14)(H) and (I))

#### Non-Manufacturing Exemptions

##### Headquarters Facility

Eligibility exists for a partial credit for building materials and equipment used for construction of a new, expanded, or remodeled headquarters facility. The taxpayer or lessor to the taxpayer must invest either:

- + A minimum of \$50 million in a building or buildings, either newly constructed, expanded, or remodeled, or
- + A minimum of \$20 million in a building or buildings, either newly constructed, expanded, or remodeled along with the creation of not less than 200 new full-time employee jobs, created during the investment period with average wages or salaries equal to, or greater than, two hundred percent of the average wage in the county or metropolitan statistical area in which the taxpayer is located.

The investment may include the purchase price of existing buildings, the cost of building materials, labor, equipment, parking facilities, and landscaping, but will not include land or inventory.

The completed facility must house the corporation's international, national, or regional headquarters. To be eligible for this credit, the corporation must apply for, and receive, authorization from the Department of Revenue.

*Effective July 1, 2004, a taxpayer that has qualified for the headquarters tax credit or an affiliate of such taxpayer can enjoy a sales and use tax exemption for "private communication services" used for communication with its computer or telecommunications center located in Tennessee. To make purchases of private communication services without the payment of sales tax, the taxpayer must provide sellers a copy of an exemption certificate issued by the Department of Revenue. (Public Chapter 782, Acts of 2004)*

*Also effective July 1, 2004, sales of telecommunications between members of an affiliated group, where one member has qualified for the headquarters sales tax credit, are exempt from sales tax. The member purchasing and selling the telecommunications services to the other members of the affiliated group is the consumer of the telecommunications services and will pay appropriate sales tax on its purchases of such services. (Public Chapter 782, Acts of 2004)*

*Effective June 7, 2004, companies that establish a new headquarters facility in Tennessee may move their otherwise taxable aircraft into the state without incurring use tax liability on those aircraft. This provision expires on July 1, 2008. (Public Chapter 924, Acts of 2004) (Tenn. Code Ann. Section 67-6-224)*



## SALES OR USE TAX

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### OTHER EXEMPTIONS FROM SALES OR USE TAX

Many products and services are identified as exempt in the sales or use tax law. The sale of these items or services requires no special documentation between the seller and buyer. A number of them are identified below. If you have questions about specific exemptions, please contact Taxpayer Services.

#### Aircraft Parts and Supplies (Tenn. Code Ann. Section 67-6-302)

- + Charges for the sale, use, or storage of aircraft owned or leased by commercial air carriers primarily for use in interstate or international commerce and parts and supplies for servicing them. This does not apply to fuel, petroleum products, or shop tools. Dealers should maintain documentation of buyer's eligibility.
- + Payments on leases or rental of property, owned by airport authorities, to businesses primarily engaged in the repair of aircraft owned or leased by commercial air carriers.

#### Amusements (Tenn. Code Ann. Section 67-6-330)

- + Events held for, or sponsored by, schools in grades K-12 or athletic events for participants 18 years old or younger sponsored by civic or nonprofit organizations.
- + Admissions to county fairs and participation in fair activities such as rides, shows, or grandstand events.
- + The first \$150 of annual dues paid to community service organizations and recreation clubs, other than country clubs.
- + Admission to museums, historical sites, and historical societies operated by nonprofit entities.
- + Fees resulting from the production of film, television, radio, or theatrical presentations. Charges for admission to these presentations are not exempted by this provision.
- + Receipts from coin-operated amusement devices.
- + Admissions to recreational or amusement facilities operated and controlled by city or county governments.
- + Member assessments made for capital improvements by recreation, community, or country clubs.
- + Proceeds from and entry fees to rodeos and beauty pageants, conducted by nonprofit organizations, which have been held in the same city for 30 years or longer.

- + Admissions to musical concerts conducted solely by nonprofit community group organizations.
- + Events held entirely by employers and solely for the benefit of their employees.
- + Dues and fees paid to physical fitness facilities that meet certain program and staffing requirements established by law, if the exemption has been approved in advance by the Department of Revenue.
- + Entry fees for any contest, tournament, or charity horse show. Fishing tournament registration fees are also exempt.

#### Automobiles

- + Automobiles sold and registered in Tennessee to members of the armed forces stationed at specific military bases located partially or wholly in Tennessee. (Tenn. Code Ann. Section 67-6-303)
- + Transfer of automobiles between spouses as the result of a divorce. (Tenn. Code Ann. Section 67-6-306)
- + Motor vehicles sold in Tennessee but removed from the state within three days and registered outside the state. (Tenn. Code Ann. Section 67-6-343)
- + Equipment used to adapt motor vehicles for use by honorably discharged disabled veterans of the armed services of the United States. (Tenn. Code Ann. Section 67-6-353)
- + *Effective June 8, 2004, sales of motor vehicles to members of the Tennessee National Guard and reserve members of a uniform service of the United States who are called into active military service and who are stationed outside the United States during hostilities in which such person is actually engaged in combat. The motor vehicle may be purchased on a power of attorney on behalf of the member. A copy of the military orders must be provided to the dealer. (Tenn. Code Ann. Section 67-6-303, amended by Public Chapter 842, Acts of 2003)*

#### Caskets and Burial Vaults (Tenn. Code Ann. Section 67-6-329)

- + Caskets and burial vaults are exempt for the first \$500 of the sales price per burial.

#### Design Professionals (Tenn. Code Ann. Section 67-6-354)

- + Concept sketches, drawings, and models made by architects, engineers, landscape architects, and interior designers used to develop a prototype for production.

## SALES OR USE TAX

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### OTHER EXEMPTIONS FROM SALES OR USE TAX (cont'd)

#### Display Property (Tenn. Code Ann. Section 67-6-305)

- + Items of inventory used by a dealer for display or demonstration that are returned to inventory within 120 days. Items consumed in display or demonstration or remaining out of inventory for more than 120 days are subject to the use tax. The dealer will pay use tax on the amount that the cost to the dealer exceeds the sales price of the article at the time it is sold.

#### Energy

- + Money paid by customers of city and county utilities, and electric cooperatives or electric membership cooperatives, which is directed to capital construction. (Tenn. Code Ann. Section 67-6-332)
- + Charges for gas, electricity, or other energy fuels sold directly to consumers for residential use. (Tenn. Code Ann. Section 67-6-334)

#### Exemptions for Tennessee Sales for Out-of-state Consumer Use

- + Sale or use of materials for fabrication of structural metal products for use on out-of-state jobs. (Tenn. Code Ann. Section 67-6-339)
- + Sale of boats or other marine vessels moved to another state within three days of purchase.
- + Sales to non-residents of helicopters and airplanes that will have a situs out of Tennessee and will be removed from Tennessee within 15 days of purchase. (Tenn. Code Ann. Section 67-6-313)
- + *Effective May 5, 2004, the sale of helicopters within Tennessee to purchasers who are not Tennessee residents are exempt when those helicopters remain in Tennessee after the sale solely for purposes of repair or refurbishment and are removed from Tennessee within 15 days of the completion of such repair or refurbishment. Repair and refurbishment includes modifications, conversions, and installations. This exemption works in conjunction with existing exemptions for the sale and repair of helicopters that are removed from the state within 15 days. (Tenn. Code Ann. Section 67-6-313(h), amended by Public Chapter 724, Acts of 2004)*
- + Repair and refurbishment services within Tennessee on airplanes and airplane components and parts, performed pursuant to a "supplemental type certificate" issued to the

repairer by the FAA, where the airplane is situated outside of Tennessee and is removed from Tennessee within 15 days from the completion of the repair. (Tenn. Code Ann. Sections 67-6-313, 345)

- + Sales of fuel and petroleum products to air common carriers for flights destined for, or continuing from, outside the United States. (Tenn. Code Ann. Section 67-6-349)
- + Sales of computer media exchange services or other storage media when that media is to be shipped out of Tennessee or to a government agency or non-taxable business in Tennessee. (Tenn. Code Ann. Section 67-6-313)
- + Sales of property for use by commercial marine vessels when the deliveries are made mid-stream in waterways that are part of the geographical boundaries of Tennessee. (Tenn. Code Ann. Section 67-6-326)
- + Repair services, including parts and labor, performed on certain types of tangible personal property, when the repair services are initiated and/or completed in Tennessee, where the repaired property is delivered or shipped out of state. This exemption applies to repairs to mining, logging, and other natural resource extraction equipment; road building equipment; land clearing, excavation, and construction equipment; and equipment for loading or unloading containers or truck trailers from railcars, ships, barges or aircraft. (Tenn. Code Ann. Section 67-6-313(b))
- + Repair service labor on aircraft engine equipment and aircraft mainframes, when the repair services are initiated, performed, or completed in Tennessee. "Aircraft engine equipment" and "aircraft mainframes" are defined by statute and limited to aircraft used by a commercial interstate or international air carrier. (Tenn. Code Ann. Section 67-6-313(c))
- + Repair services, including parts and labor, performed out of state on equipment used primarily in interstate commerce, when the original purchase of the equipment was exempt from sales and use tax. (Tenn. Code Ann. Section 67-6-313(d))
- + Repair parts and labor for firefighting equipment owned by an out-of-state fire department. (Tenn. Code Ann. Section 67-6-313(e))
- + Repair service labor on railroad rolling stock, when the repair services are initiated, performed, or completed in Tennessee. (Tenn. Code Ann. Section 67-6-313(g))
- + Parts and accessories, materials and supplies used in servicing and/or maintaining railroad rolling stock used, or intended to be used, in interstate commerce. (Tenn. Code Ann. Section 67-6-321(a))

## SALES OR USE TAX

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### OTHER EXEMPTIONS FROM SALES OR USE TAX (cont'd)

- + The transfers of railroad rolling stock and vessels or barges of 50 tons or more displacement that are used in interstate commerce or outside Tennessee. (Tenn. Code Ann. Section 67-6-321)
- + Repair services, including renovations and improvements, performed on barges and vessels of 50 tons and over displacement, used in interstate commerce, and the parts, accessories, material, and supplies used in such repairs if the parts, accessories, material, and supplies become a part of the barge. (Tenn. Code Ann. Sections 67-6-321, 327)

### Films (Tenn. Code Ann. Section 67-6-309)

- + Rental fees of films to theaters that charge tax on admission prices to view the films.
- + Rental prices for films, recordings, or transcriptions charged to radio and television stations operating under license by the Federal Communications Commission.

### Food (Tenn. Code Ann. Sections 67-6-337, 338)

- + Food paid for by food stamps or vouchers from special supplemental food programs for women, infants, and children as required by federal law, or any other means approved by the Department of Human Services and issued by the department or the federal government.

### Fuel (Tenn. Code Ann. Section 67-6-329)

- + Motor vehicle fuels taxed per gallon under the petroleum products provisions of Tennessee law.
- + Gasoline on which a privilege tax is paid.

### Leased Vehicles

- + *Effective June 6, 2004, insurance proceeds paid to the owner of a leased vehicle pursuant to a damage settlement are exempt. The exemption applies when the vehicle has sustained damage that renders it a salvage vehicle, a nonrepairable vehicle, or a flood vehicle, and the owner transfers title of the leased vehicle to the insurance company. (Tenn. Code Ann. Section 67-6-388, enacted by Public Chapter 832, Acts of 2004)*

### Medical Equipment and Supplies

- + Sales of human blood and plasma. (Tenn. Code Ann. Section 67-6-304)
- + Sales of insulin and the syringes to administer the insulin. (Tenn. Code Ann. Section 67-6-312)
- + Oxygen prescribed for medical treatment of a human being and the equipment to administer it. (Tenn. Code Ann. Section 67-6-318)
- + Ostomy products or appliances used by persons with colostomies, ileostomies, or urostomies. (Tenn. Code Ann. Section 67-6-317)
- + Sales and maintenance of artificial limbs and the items needed to wear them, handicap lift devices that allow entrance and exit from motor vehicles, wheelchairs for handicapped persons, and prosthetics, including pacemakers. (Tenn. Code Ann. Section 67-6-314)
- + Sale and repair of prosthetics and orthotics such as orthopedic shoes, walkers, crutches, and similar medical corrective or support devices. (Tenn. Code Ann. Section 67-6-314)
- + Sale of disposable medical supplies used for the intravenous administration of prescription medications outside of a hospital or other medical facility. (Tenn. Code Ann. Section 67-6-320)
- + Sale of computer software, prescribed by a practitioner of the healing arts, designed for the treatment of people with learning disabilities. (Tenn. Code Ann. Section 67-6-314)
- + Sale and repair of hearing aids. (Tenn. Code Ann. Section 67-6-329)
- + All veterinary drugs are taxable to the veterinarian at cost except for livestock medication and wormers, which are totally tax-exempt. (Tenn. Code Ann. Section 67-6-351)
- + Repair parts and services for helicopters and aircraft used by government organizations and nonprofit hospitals and medical facilities for medical evacuation or transportation. (Tenn. Code Ann. Section 67-6-347)
- + Prescription drugs distributed free of charge by the manufacturer. (Tenn. Code Ann. Section 67-6-319)
- + Prescription drugs or medicines issued by pharmacist and prescribed by practitioners of the healing arts for human consumption. (Tenn. Code Ann. Section 67-6-320)

### Miscellaneous Nonprofit Sales

- + Sales at gun shows conducted by a nonprofit organization of gun collectors. Sales by dealers who regularly conduct gun sales, and sales of guns for later delivery are not tax exempt. (Tenn. Code Ann. Section 67-6-310)
- + Sales of schoolbooks and school lunches. (Tenn. Code Ann. Section 67-6-329)



## SALES OR USE TAX

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### OTHER EXEMPTIONS FROM SALES OR USE TAX (cont'd)

- + Sales of parking privileges sold by colleges, universities, technical institutes, or technology centers to students. (Tenn. Code Ann. Section 67-6-329)
- + Sales of United States or Tennessee flags by nonprofit organizations. The amount of the exemption is equal to the cost of the flags to the organization. (Tenn. Code Ann. Section 67-6-329)

### Motor Vehicles Used by Common Carriers (Tenn. Code Ann. Section 67-6-331)

The transfer, by any dealer in personal property, of motor vehicles with a Gross Vehicle Weight Rating of Class 3 (maximum gross weight of vehicle and load of 20,000 pounds) (Tenn. Code Ann. Section 55-4-113) and above, and trailers, semi-trailers, and pole-trailers (Tenn. Code Ann. Sections 55-1-105, 55-4-113) that will be used to transport passengers or cargo principally in interstate or foreign commerce, by a common carrier or contract carrier under authority granted by the federal government or other state regulatory agency, shall be exempt from the sales or use tax. The term "principally" means more than 50% use. *Effective June 7, 2004, this exemption is available regardless whether or not the carrier sells its services for a fee, provided that all requirements of Tenn. Code Ann. Section 67-6-331 are met.*

A motor vehicle is used to transport cargo or passengers in interstate or foreign commerce if it transports passengers or cargo from:

- + A point of origin in another state or foreign country to a point within this state.
- + A point of origin within this state to a point in another state or foreign country.
- + A point of origin in another state or foreign country, moving through Tennessee, to a point in a different state or foreign country.

### Packaging

- + Containers and packaging materials actually accompanying products sold, without which their delivery would be impracticable on account of their character, and for which there is no separate charge, are exempt from sales or use tax. (Tenn. Code Ann. Section 67-6-102(28)(E)(ii))

### Pollution Control

- + Sales of chemicals and supplies used in air and water pollution control. (Tenn. Code Ann. Section 67-6-346)

### Preservation of Historic Property

- + *Effective June 3, 2004, a sales or use tax exemption exists for tangible personal property or taxable services sold, given, or donated to an entity that is directly or indirectly owned and controlled by a nonprofit entity, is organized for the purpose of preserving or rehabilitating a historic property listed on the National Register of Historic Places, and the controlling nonprofit entity has received approval of its historic certification application by the U.S. Department of the Interior National Park Service. (Tenn. Code Ann. Section 67-6-322 as amended by Public Chapter 812, Acts of 2004)*

### Publications

- + Magazines and books distributed to consumers via the United States Postal Service or common carriers by sellers or distributors whose only Tennessee activities involve the printing, storing, labeling, or delivering of these items to the postal service or common carrier, maintenance of stock or newsgathering activities. (Tenn. Code Ann. Section 67-6-329)
- + Publications printed on newsprint or bond paper and advertising supplements or other printed inserts delivered with the publications on a biweekly or more frequent basis. (Tenn. Code Ann. Section 67-6-329)
- + Direct mail advertising, in the form of discount coupons or advertising leaflets for more than one business, distributed in Tennessee from out of state. (Tenn. Code Ann. Section 67-6-344)

### Sales in Interstate Commerce

- + When title and possession of property passes from seller to buyer outside Tennessee, the sale is considered to be in interstate commerce. These sales are exempt from state and local sales or use tax in the state where the seller is located.

### Telephone Cooperatives

- + Sales of tangible personal property to telephone cooperatives organized under Tennessee law, for their own use or consumption. (Tenn. Code Ann. Section 67-6-325)

## SALES OR USE TAX

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### OTHER EXEMPTIONS FROM SALES OR USE TAX (cont'd)

#### Telecommunications

- + Charges made by local telephone exchanges to long distance resellers and cellular telephone companies for local access and use of intercompany facilities. (Tenn. Code Ann. Section 67-6-342)
- + *Charges for Internet access or information services are not subject to sales and use tax. (Tenn. Code Ann. Section 67-6-102(a)(32), amended by Public Chapter 782, Acts of 2004)*

#### Transactions Between Parent Companies and Wholly Owned Subsidiaries

- + The sale, transfer, or lease of construction machinery between parent companies and wholly owned subsidiaries is not taxable provided the Tennessee sales or use tax was paid on the property at its initial purchase. (Tenn. Code Ann. Section 67-6-311)
- + Services, which would otherwise be taxable, are not subject to the sales tax if the corporations involved meet certain ownership and control requirements. The services must not be performed for profit. (Tenn. Code Ann. Section 67-6-350)

#### Used Property

- + Sales of used factory-manufactured structures to the extent the Tennessee sales or use tax was paid on the initial purchase of the structure in Tennessee. (Tenn. Code Ann. Section 67-6-336)
- + Retail sales of used clothing by 501(c)(3) nonprofit organizations that have been issued a certificate of exemption by the Commissioner of Revenue. (Tenn. Code Ann. Section 67-6-348)

#### Vending Items

- + The proceeds of vending machines operated for the benefit of a charitable non-profit organization by which merchandise of the market value of not more than 25 cents is sold or delivered to customers are subject to a gross receipts tax of 1.5% rather than the sales or use tax. (Tenn. Code Ann. Section 67-4-506)

#### Warranty Services

- + Parts supplied to consumers for replacement, under warranty, of faulty parts are not taxable if the sales or use tax was originally paid on the item under warranty. (Tenn. Code Ann. Section 67-6-324)

#### Watershed Districts

- + Sales of tangible personal property for use by watershed districts. (Tenn. Code Ann. Section 67-6-328)

## SALES OR USE TAX

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### FLEA MARKETS

#### **Flea Market Registration (Tenn. Code Ann. Sections 67-6-102, 220)**

Dealers who sell at flea markets will register and pay an annual registration fee of \$45. This registration fee shall be credited against that person's actual annual sales tax liability. This registration shall be valid at any location in the state during the period for which it is issued.

#### **Sales on Less than Permanent Basis**

Dealers engaging in retail sales at flea markets on less than a permanent basis may register, at their option, as follows:

(A) On a quarterly basis for a fee of \$15. This registration fee is to be paid per location at which retail sales are made. A person may register a maximum of three times per year at each location. A dealer, needing to register more than three times per year at any one location, must purchase an annual registration certificate. No refund is payable from the registration fee. This registration fee shall, however, be credited against any such person's actual sales tax liability.

(B) On a monthly basis for a fee of \$5. This registration fee is to be paid per location at which retail sales are made. A person may register a maximum of three times per year at each location. A person needing to register in excess of three times must purchase either a quarterly or an annual registration certificate. No refund is payable from the registration fee. This registration fee shall, however, be credited against any such person's actual sales tax liability.

The flea market operator is responsible for ensuring that all dealers operating at the flea market are properly registered with the department. The flea market operator is empowered to accept applications for registration with all required fees. The operator will supply the dealer with a copy of the application for registration, together with evidence of the amount of fee submitted. This copy shall be

displayed by the dealer and shall serve as evidence of proper registration

The provisions of this section do not apply to dealers who sell prepared foods at flea markets for consumption.

#### **Submission of Flea Market Returns (Tenn. Code Ann. Sections 67-6-102, 220)**

#### **Dealers Registering Annually**

If the annual sales tax liability is less than \$45 for a dealer registering annually, that person is not required to file an annual sales tax return. In no case will any person receive a refund of any portion of the registration fee. Should any dealer's tax liability exceed \$45, then that dealer will file an annual return. The return will be due by January 20 and reflect the gross sales during the preceding calendar year. A dealer beginning business after January 1 will be responsible for transmitting an annual return on or before January 20 of the subsequent calendar year for all months in which the dealer made taxable sales or purchases through December 31 of the preceding year.

#### **Dealers Registering Quarterly or Monthly**

Dealers registering on a quarterly or monthly basis shall file quarterly returns if their tax liability exceeds the amount of the registration fees paid during that quarter. The quarterly returns will be due by the 20<sup>th</sup> day of the next month following the end of each quarter and will show the gross sales from all taxable sales or purchases during the preceding quarter.

At the time of transmitting any of the returns, the dealer shall remit the amount of tax due. Failure to so remit the tax or to file the return will make the tax delinquent. Failure to remit the tax or to file the return will subject the dealer to penalties and interest and the possibility of further actions.

#### **Penalty For Late Filing**

The flea market operator will submit the registration fees collected on the operator's monthly return to the commissioner, together

## SALES OR USE TAX

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### FLEA MARKETS (cont'd)

with the registration applications received by the operator. Failure to comply will subject the flea market operator to the penalty provided by law for delinquent tax payments.

The penalty to the dealer will be \$10 per booth per day for violations of tax remittance requirements. The department may also impose a penalty upon the flea market operator of \$10 per booth per day, up to a maximum fine of \$100 per day at any location where it is determined by the commissioner that the flea market operator has been negligent in allowing dealers to operate at the flea market without proper registration.

The term “negligent” includes, but is not limited to, any failure of the flea market operator to make a reasonable attempt to ensure that every dealer renting space from the operator is properly registered for tax purposes. A determination by the commissioner that a flea market operator has been negligent shall be deemed presumptively correct. Such determination may be rebutted only if the flea market operator makes a showing of due care. As used, “due care” means that the flea market operator has made every reasonable effort to ensure that every dealer renting space from the operator is properly registered for tax purposes.

## SALES OR USE TAX

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### CONTRACTORS

Generally, contractors are persons who perform installations of personal property as an improvement to realty. Contractors may include persons performing management services. The term “contractor” also includes subcontractors as well.

#### **Contractors as Consumers (Tenn. Code Ann. Section 67-6-209)**

Contractors and subcontractors who improve realty, or otherwise use personal property in the performance of a contract, are considered the users and consumers of the materials that are used or installed as part of the real property. If the sales tax is not paid when the materials are purchased, the contractor or subcontractor owes the use tax on the cost of their materials. The labor costs of installation or erection and markup on materials are not taxable. The sales or use tax cannot be itemized separately and collected from the contractee.

#### **Liability for the Sales or Use Tax**

Generally speaking, the contractor or subcontractor remains liable for the sales or use tax on materials used in providing the contracted service even when the contractee is an otherwise exempt entity, such as federal, state, county, or city governments, and most exempt organizations. This is true even when the tax-exempt entity buys the materials and turns them over to the contractor or subcontractor for use.

A contractor-dealer is one who improves realty and is also engaged in selling building materials and supplies to other contractors, consumers, or users. Materials that may be sold at retail to other users can be purchased on a resale certificate; sales tax will be collected and remitted on the retail sales.

Contractor-dealers who cannot separate the portions of their materials and supplies that they will consume in fulfillment of their contracts and those they will resell to other consumers may give a resale certificate to the seller of their materials and supplies. The contractor-dealer will then report sales tax on the materials resold

and use tax on the materials used in fulfillment of their contracts.

Suppliers making sales to contractor-dealers and delivering the materials to a job site for use by the contractor-dealer, or tagging particular supplies for a particular job performed by the contractor-dealer, must collect the applicable sales tax on those sales, even if the contractor/dealer presents a certificate for resale. (Sales Tax Rule 1320-5-1-.08)

#### **Exemptions (Tenn. Code Ann. Sections 67-6-102, 209, 384)**

Under specific circumstances outlined in the law, contractors or subcontractors are not liable for the sales or use tax on construction materials. These specific exemptions are:

- + If materials are purchased by a church and are used in church construction, the materials are exempt from both state and local sales or use tax. Similarly, carpet installed by a contractor for church construction is exempt.
- + If materials are purchased by a private, nonprofit college or university and are used in college or university construction, they are exempt from the state sales or use tax but not from the local tax.

Specific exemptions from sales or use tax are available to contractors for specific types of contracts. Examples are:

- + Electrical generating facilities and distribution systems owned by a government entity.
- + Wastewater and sewage systems, and sanitary sewer pipes owned by a county or city.
- + Coal gasification plants and distribution systems owned by government entities.
- + A neutron spallation facility owned by the federal government.

#### **Tax on Fabricated Materials**

Contractors fabricating raw materials for use in building construction are liable for the sales or use tax on the cost of the raw materials. On the other hand, contractors fabricating materials for use in non-building projects, such as bridge steel, are liable for tax on the fabricated value of the materials.

## SALES OR USE TAX

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### CONTRACTORS (cont'd)

#### Asphalt Fabricators

Asphalt fabricators must remit use tax based on the fair market value of asphalt they use in fulfilling their contracts. The tax amount must be computed on the amount the fabricator would charge for the asphalt if it were sold and delivered in an arms length transaction. The Department of Revenue will accept as fair market value \$5 per ton plus the cost of materials as the tax base.

Asphalt fabricators that sell asphalt to other contractors or customers without performing installation and who also install asphalt may purchase their materials on a certificate of resale. The asphalt contractor must collect sales tax on the total sales price of the asphalt fabricated and sold to other contractors. If the asphalt fabricator uses the asphalt rather than sells it, the asphalt fabricator will owe the use tax as previously indicated.

Use of asphalt by an asphalt fabricator or installer in a contract with a government or other tax-exempt entity subjects the fabricator or installer to payment of the use tax. Use tax is due even if the asphalt is provided by the government or tax-exempt entity. However, if asphalt is sold directly to the exempt entity with no installation or use by the seller, the purchase is tax-exempt. (Tenn. Code Ann. Section 67-6-209 and Tenn Comp R. & Regs 1320-1-1.03(1)(a))

#### Installation of Industrial Machinery

Contractors installing qualified tax-exempt industrial machinery for qualified manufacturers must apply to the Department of Revenue for their own industrial machinery authorization number for each project.

#### Lump Sum or Unit Price Construction Contracts on Realty in Effect on July 15, 2002

All construction contractors and subcontractors will pay to their vendors the increased state tax of 7% on materials purchased on or after July

15, 2002. Vendors of materials who have a lump sum or fixed price contract to provide materials are required to collect and remit the new rate of tax.

General or prime construction contractors making improvements to real property under a lump sum or unit price construction contract entered into prior to July 15, 2002, or contracts awarded by the state or a political subdivision pursuant to a bid opening which occurred prior to July 15, 2002, if the provisions of such provide that the amount payable remains fixed without regard to costs, may file a claim for refund with the Department of Revenue for tax paid to any of the contractor's vendors at a rate in **excess** of the 6% state rate and the applicable local option sales tax in effect July 1, 2002. A claim for refund must be supported by a copy of the contract that was signed prior to July 15, 2002, and documentation in the form of schedules and invoices to support the payment of sales tax in excess of the 6% state rate. A separate claim form will be required for each contract.

Subcontractors entering into lump sum or unit price contracts to make improvements to realty prior to September 1, 2002, with general or prime contractors that have entered into contracts described in the preceding paragraph prior to July 15, 2002, may file a claim for refund with the Department of Revenue for tax paid in excess of the 6% state rate and the applicable local option sales tax in effect July 1, 2002. A claim for refund must be supported by a copy of the subcontractor's contract that was signed prior to September 1, 2002, a copy of the contractor's contract entered into prior to July 15, 2002, and documentation in the form of schedules and invoices to support the payment of sales tax in excess of the 6% state rate. A separate claim form will be required for each contract.

Effective January 27, 2003, contractors and subcontractors who have made purchases without the payment of tax on tangible personal property that will be used in the performance of qualifying lump sum or unit price construction contracts that became binding prior to July 15,

## SALES OR USE TAX

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### CONTRACTORS (cont'd)

2002, should report and remit the use tax at the 6% state rate and the applicable local option tax rate. Dealers are required to keep records to demonstrate the tangible personal property was subject to the 6% state rate. Such records include a copy of the contract with the dates that the contract was entered into, records indicating the materials used in the performance of the qualifying lump sum contract, and records demonstrating that the state rate of 6% and the applicable local tax rate was reported and paid to the department

“Lump sum or unit price construction contract” is defined as a written contract for the construction of, or improvements to, real property under which the amount payable to the contractor, subcontractor, or material vendor is

fixed without regard to costs incurred in the performance of the contract.

#### ***Property Owned by the United States Government***

*Effective May 19, 2004, an exemption from contractor's use tax is available for any tangible personal property that is owned by the United States and is provided to a contractor on a temporary basis to be tested, provided that the exemption applies only to contracts awarded under the Small Business Innovation Research Program, and does not apply to equipment or other property used to conduct the test. (Tenn. Code Ann. Section 67-6-209, amended by Public Chapter 725, Acts of 2004)*



## SALES OR USE TAX

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### RETURNS AND PAYMENTS

#### **Returns and Payment (Tenn. Code Ann. Sections 67-6-504 – 506)**

After completing the registration process, you will receive reporting information. A computer generated sales or use tax return will be mailed to you monthly unless otherwise instructed. You must file a timely return, beginning with the date entered in Item 4 of the application, even if no sales were made and no tax is due.

Sales or use taxes are due on the first day of each month for the preceding month. The last day for returns to be timely filed with the Department of Revenue, on forms provided by the department, is the 20<sup>th</sup> of each month. The amount of tax due will be sent with the return. Failure to do so will make the return delinquent. The postmark date on the envelope in which the return is mailed is considered the filing date.

The commissioner may decide, when it is in the best interest of the state, that specific taxpayers may file returns on other than a monthly basis. The commissioner may also, under emergency or extraordinary reasons, extend a taxpayer's time for filing a return for up to 30 days. In the latter case, any interest payment will be added to the amount of payment due.

If a taxpayer has paid a legally imposed sales or use tax to another state for property imported into this state, that payment may be claimed as a credit against the tax on the Tennessee return. The taxpayer must be able to furnish the name of the vendor from whom the property or service was purchased and an affidavit or bill of sale showing the tax has been paid. (Tenn. Code Ann. Section 67-6-507)

If a taxpayer fails to report and pay the sales or use tax as required or files a grossly incorrect or fraudulent report, the commissioner will estimate the amount of tax due plus interest and penalties, if applicable, and the taxpayer will be assessed accordingly. (Tenn. Code Ann. Section 67-6-517)

#### **Electronic Data Interchange (EDI)**

The Electronic Data Interchange program is a method of filing tax returns electronically from one computer to another. Tennessee sales or use tax taxpayers that are required to make their tax payments by Electronic Funds Transfer are required to file their returns through EDI. Taxpayers that choose to voluntarily file their returns via EDI must remit their tax payments electronically. All other Tennessee sales or use tax taxpayers have the option of filing their returns through EDI.

The EDI setup involves several steps including selecting a certified software vendor or Internet tax service provider, completing the registration process, establishing communications, and performing a test of the chosen software. It is the taxpayer's responsibility to choose a software vendor. Internet tax services provide or develop its own software.

Each taxpayer that files sales tax returns electronically must have a Registration for Sales Tax Electronic Filing Application on file with the Department of Revenue. If using a software vendor, the taxpayer must also complete a Transmission Specification Questionnaire for the department. Additionally, each taxpayer that pays sales taxes electronically must have an Electronic Funds Transfer (EFT) agreement on file with the department. Taxpayers who file electronically must pay electronically.

Software vendors and Internet tax services usually offer both "Filing Only" and "Filing and Payment" options. If the "Filing Only" option is selected, the software or tax service will only initiate a transaction for filing the return. The associated EFT payment will need to be initiated via the department's EFT program.

To avoid late delivery of the return and payment, taxpayers using a tax service must contact their provider for cutoff deadlines. Taxpayers using software must transmit to the department's filing service by 4:15 p.m., Eastern Time, on the



## SALES OR USE TAX

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### RETURNS AND PAYMENTS (cont'd)

business day prior to the due date for "Filing and Payment" transactions, and by 11: 59 p.m., Eastern Time, on the due date for "Filing Only" transactions.

#### Electronic Funds Transfer (EFT)

The Tennessee General Assembly has authorized the Commissioner of Revenue to require certain tax payments to be made by funds readily available to the state. Electronic Funds Transfer is a method approved by the Commissioner for accomplishing this. Rules for the administration of this legislation went into effect on January 1, 1992.

Two payment options are available that use the Automated Clearing House (ACH) system to electronically transfer tax payments. The ACH system is a nationwide network designed for this purpose and is the preferred transaction method for many financial institutions and corporations. A third payment option, Federal Wire Transfer, should be used only as an emergency option.

Penalty and interest charges may be incurred if the taxpayer fails to remit by the chosen method. No matter which method is chosen, the taxpayer must complete the Electronic Funds Transfer Agreement with the Department of Revenue.

The department will notify taxpayers that they are required to file electronically if the taxpayer's average payment is \$10,000 or more. A taxpayer may also choose to participate voluntarily when not required to do so. Voluntary participants are subject to the same rules and regulations as persons required to participate.

Additional information on EDI and EFT, and the required forms, may be obtained by contacting the Department of Revenue's Electronic Commerce Unit at (615) 741-5876.

#### Online Filing

*Another option for filing returns is online filing through the state's Web portal. Online filers can file all periodic returns and make payments directly from checking accounts. They can also*

*update business information, such as location and mailing addresses. They can also file past due and amended returns. Returns can be filed right up to midnight of the return due date to ensure timely filing. Online filing will also calculate the return and provide an immediate confirmation of receipt by the Department of Revenue. Online filing is free without purchasing additional software. Information about initiating online filing is available on the department's Web site.*

#### Mailing Date

If the due date for a return falls on Saturday, Sunday, or a holiday, the due date is automatically extended until the next business day. Returns mailed through the United States mail will be considered filed and received on the date shown by the post office cancellation mark on the envelope. If the cancellation mark is not legible or is missing, then the return will be considered filed on the date the envelope is stamped as "Received" by the Department of Revenue. (Tenn. Code Ann. Section 67-1-107)

#### Penalty and Interest

A penalty is imposed for the late filing of a tax return and for late payment of taxes owed the state. The penalty is computed at a rate of 5% per month, or any portion of a month, from the due date until the date the taxes are paid. The maximum penalty is 25% of the tax amount due; the minimum penalty is \$15.

Interest is imposed on any taxes not paid by the date required by law even though a filing date extension has been granted. The interest rate on deficient tax payments is established on July 1<sup>st</sup>.

When a taxpayer fails to submit a timely return and penalties and/or interest are applied, the penalties and interest become a part of the tax due. The Department of Revenue has no discretion to refund or waive any interest charges. (Tenn. Code Ann. Section 67-1-804)

## SALES OR USE TAX

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### RETURNS AND PAYMENTS (cont'd)

#### Audits and Assessments

All tax returns filed with the Department of Revenue undergo some type of audit or examination to ensure that the correct tax has been paid. This may be a computer math audit, a manual examination by a trained auditor, or both. The taxpayer will be contacted if additional information is needed to complete the audit. The taxpayer will receive written notification of any adjustments made to the return.

Taxpayers selected for field audits will be contacted by the department to set up a convenient time for the audit. Taxpayers will receive advance notice of which records will be needed for the audit. A field audit generally involves examination of documentation and records used to file returns for three previous years.

At the completion of the audit, the auditor will leave the taxpayer a written report for review. Once the auditor has made any necessary changes to the report, the notice of assessment for any underpaid taxes will be issued. (Tenn. Code Ann. Section 67-1-1301)

#### Right to a Conference (Tenn. Code Ann. Section 67-1-1801)

Taxpayers are entitled to an informal conference to discuss an assessment. If this request is made in writing within 30 days from the date of the Notice of Assessment, the conference must be granted. If made after 30 days, the conference may be granted at the commissioner's discretion.

Taxpayers wishing to contest an assessment without making payment have 90 days following the mailing of the notice of assessment to file suit in chancery court, as provided by statute. Interest will continue to accrue at the prevailing rate until payment is received. A lien may be filed against the taxpayer's property during this 90-day period, but the department generally may not levy on the taxpayer's property to satisfy the assessment.

If the taxpayer timely requests an informal conference, the 90-day period for filing suit stops running until a conference decision is issued in writing. After the decision is issued, the 90-day period recommences. The 90-day stay for most collection activity is likewise extended. The taxpayer is not required to request an informal conference before contesting an assessment in court.

If the taxpayer does not file suit within the 90-day period to contest the assessment, the taxpayer may pay the assessment, request a refund, and then file suit in chancery court within six months from the date the request is denied or deemed denied by operation of law. Procedures outlined in Tenn. Code Ann. Section 67-1-1802 must be followed.

#### Keeping Records

Taxpayers are required to establish and maintain records that are adequate for auditors to use in determining the correct amount of a business's tax liability. This responsibility includes not only those liable for sales tax but also businesses or individuals subject to use tax – persons importing untaxed tangible personal property for storage, use, or other consumption in the state. Records of business transactions must be kept for a minimum of three years and must include:

- + A daily record of all cash and credit sales including those under a finance or installment plan.
- + A record of the amount of all merchandise purchased including bills of lading, invoices, and purchase orders.
- + A record of all deductions and exemptions allowed or claimed including exemption and resale certificates.
- + A record of all property used or consumed in the conduct of the business.
- + A true and complete yearly inventory of the value of stock on hand.

All such records shall be open for inspection, at all reasonable hours, to the Commissioner of Revenue or authorized representatives of the commissioner. (Tenn. Code Ann. Section 67-6-523)

If the taxpayer maintains any such records in an electronic format, the taxpayer shall comply with reasonable requests by the commissioner, or the commissioner's authorized agents, to provide those electronic records in a standard record format. (Tenn. Code Ann. Section 67-1-113)

## SALES OR USE TAX

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### THE TAXPAYER BILL OF RIGHTS

You, as a taxpayer, have certain rights. Your rights are so important that, in 1992, the Tennessee General Assembly enacted legislation to spell them out. The Tennessee Taxpayer Bill of Rights summarizes state tax laws and revenue rules with which the Department of Revenue must comply while serving you.

#### TAXPAYER RIGHTS (Tenn. Code Ann. Section 67-1-110)

Tennessee guarantees that you, the taxpayer, have the right to:

- Fair and courteous treatment from all employees of the Department of Revenue.
- Tax forms and information written in plain language.
- Prompt and accurate responses to all inquiries and requests for tax assistance.
- Access public records not confidential or otherwise protected by law, and to review such records at an appropriate time and location.
- Obtain all tax information relating to your account, including financial information, which is kept confidential, except to the extent required by law.
- Tax notices that clearly explain the amount being billed.
- Clear rules and procedures to resolve tax problems.
- An informal conference, as provided by law, with the Commissioner of Revenue or her delegate to dispute any tax assessment. (Taxpayers have the right to be represented by an attorney, certified public accountant, or other representative at such conference).
- Assurance that employees of the Department of Revenue are not paid, promoted, or in any way rewarded on the basis of assessments or collections.
- Suggest ways the Department of Revenue may better serve the public.
- Prompt notification of any refund to which you are entitled.
- Assistance through statewide meetings held by the Department of Revenue in convenient locations in which taxpayers are allowed to ask questions and voice opinions.
- Notice and demand for payment 10 days before the Department of Revenue makes any collection effort, except as otherwise provided by law.
- 30 days notice before seized assets are liquidated, except as otherwise provided by law.

#### TAXPAYER RIGHT TO A CONFERENCE (Tenn. Code Ann. Section 67-1-1801)

Taxpayers are entitled to an **informal conference** to discuss an assessment. If this request is made in writing within 30 days from the date of the Notice of Assessment, the conference must be granted. If it is made beyond the 30 days, the conference may be granted within the discretion of the Commissioner.

Requests for conferences may be sent by mail or fax transmittal to:

Administrative Hearing Office  
Tennessee Department of Revenue  
500 Deaderick Street, Room 1240  
Nashville, TN 37242  
Phone (615) 741-3810  
Fax (615) 532-8971

## SALES OR USE TAX

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### THE TAXPAYER BILL OF RIGHTS, cont'd

Taxpayers who wish to contest an assessment without making payment have 90 days to file suit in chancery court, as provided by statute. Interest will continue to accrue at the prevailing rate until payment is received. A lien may be filed against the taxpayer's property during this 90-day period, but the department generally may not levy on the taxpayer's property to satisfy the assessment.

If the taxpayer timely requests an informal conference, the 90-day period for filing suit stops running until a conference decision is issued in writing. After the decision is issued, the 90-day period resumes running. The 90-day stay for most collection activity is likewise extended. The taxpayer is not required to request an **informal conference** before contesting an assessment in court.

If the taxpayer does not timely file suit to contest the assessment, the taxpayer may pay the assessment, request a refund, and then file suit in chancery court for a refund in accordance with the procedures set forth in Tenn. Code Ann. Section 67-1-1802.